

COMMONWEALTH OF MASSACHUSETTS
DEPARTMENT OF TELECOMMUNICATIONS AND ENERGY
WESTERN MASSACHUSETTS ELECTRIC COMPANY
DOCKET NO. D.T.E. 97-120
ELECTRIC RESTRUCTURING PLAN

TESTIMONY OF
RICHARD A. SODERMAN
ON BEHALF OF
WESTERN MASSACHUSETTS ELECTRIC COMPANY

SEPTEMBER 4, 1998

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1 **I. INTRODUCTION**

2 Q. Please state your name and business address. Please state your name, position,
3 and business address.

4 A. Richard A. Soderman, 107 Selden Street, Berlin, Connecticut 06037.

5

6 Q. Please state your position with Western Massachusetts Electric Company
7 ("WMECO or the Company").

8 A. I am Director of Regulatory Policy and Planning for Northeast Utilities Service
9 Company ("NUSCO") which provides centralized services to the operating
10 companies of the Northeast Utilities ("NU") system, including WMECO.

11

1 Q. In your position, what are your areas of responsibility?

2 A. I am responsible for developing and implementing regulatory policies and
3 practices for the NU system companies. Additional biographical information can
4 be found in Exhibit RAS-1.

5

6

7 Q. Please provide an overview of the purpose of your testimony.

8 A. The purpose of my testimony generally is to organize various information,
9 including updates and revisions, that have already been submitted by WMECO in
10 this proceeding and more specifically to support the development of: (1) the 10
11 percent rate reduction; (2) the distribution, transmission, and transition charges,
12 including the identification, mitigation and recovery of transition costs; and
13 (3) standard offer service energy charges that the Company has proposed to be
14 collected from customers as a result of implementing customer choice and
15 restructuring on March 1, 1998. Additionally, I will address the Company's
16 previously proposed deferral and true-up mechanisms that will enable WMECO to
17 meet the future requirements of the Act and continue to maintain a financially
18 stable and viable position.

19

20 Q. Will you be referring to other material in your testimony?

21 A. Yes, I will be referring to the Revised Plan and attached appendices and exhibits.
22 The Revised Plan incorporates the modifications and updates that the Company
23 has made to its restructuring plan since it was originally filed on December 31,

1 1997. Additionally, I have provided as Exhibit RAS-2 a listing of all data
2 requests in this proceeding for which I will be wholly or partially responsible for
3 supporting during the hearing process. These documents are provided with the
4 intent of facilitating the Department's review of the Company's Revised Plan in
5 this proceeding.

6
7 Q. Please provide an overview of the sections in the Revised Plan and a list of the
8 exhibits and appendices attached to it.

9 A. The Revised Plan provides a detailed narrative of the Company's proposed
10 process and response to meeting and implementing the required rate reductions,
11 customer choice, and other mandates specified by the legislation which was
12 enacted by the General Court and signed into law on November 25, 1997 (the
13 "Act"). The Revised Plan is comprised of a narrative that covers eight basic
14 elements with supporting appendices and exhibit. Attached to my testimony is
15 Exhibit RAS-3 which provides a table of contents for the narrative and a list of
16 the appendices and exhibits.

17
18 The eight basic elements of the Revised Plan are: 1) the rate unbundling process
19 and the provision of a ten percent discount for customers on March 1, 1998;
20 2) customer choice of energy supplier; 3) the solicitation process to ensure
21 provision of standard offer and default service; 4) determination and recovery of
22 transition costs; 5) mitigation of transition costs including divestiture and
23 securitization; 6) universal service and direct retail access for customers;

1 7) energy conservation and renewables funding; and 8) employee and community
2 impact issues. Each of the above elements are supported by pre-filed testimony
3 being submitted herewith.

4
5 **II. TEN PERCENT RATE REDUCTION**

6 Q. Has WMECO reduced its rates by the amount required under the Act?

7 A. Yes. On March 1, 1998, WMECO reduced its permanent rates that were in effect
8 in August 1997 by 10 percent. The Department approved this reduction on an
9 interim basis in its February 20, 1998 Order.

10
11 This rate reduction was based on rates that did not reflect a temporary rate credit
12 that expired on February 28, 1998. WMECO proposed on May 15, 1998 to
13 increase the rate reduction by the amount of the temporary rate credit if it were
14 permitted to defer for future recovery the earnings impact that this added
15 reduction would cause until securitization is implemented. The Company also
16 proposeds to securitize this deferral. On July 2, 1998 the Department approved
17 this additional reduction, but did not rule on the Company's requests for deferred
18 accounting treatment and eventual securitization of an equivalent amount of costs
19 associated with the reduction. Therefore, that issue remains pending in this
20 proceeding and WMECO requests that the Department, along with issuing a final
21 approval of the Company's two rate reductions, allow the Company to defer
22 appropriate costs related to the July 1, 1998 additional rate reduction and rule that
23 these deferred costs qualify as transition costs so that they will be eligible for

1 securitization which will be reviewed in a subsequent proceeding.

2

3

4 **III. REVENUE REQUIREMENTS OF WMECO'S UNBUNDLED RATES**

5 Q. Please describe the components of the Company's tariffs as proposed in this
6 docket.

7 A. As described in the Company's Initial and Revised Plan, the Company has
8 unbundled its tariffs into four components: Distribution, Transmission,
9 Transition, and Generation. I will describe the development of these components
10 from a revenue requirements perspective. Mr. Roncaioli more fully describes
11 how the rates have been unbundled from a tariff and billing perspective.

12

13 Distribution Revenue Requirements

14 Q. How were the 1998 Distribution revenue requirements developed?

15 A. The 1998 Distribution component was developed utilizing 1998 budgeted cost of
16 service information based on revenue requirements with a 11% return on equity.
17 The revenue requirements reflect changes in costs that have occurred since the
18 Company's last rate case (D.P.U. 91-290) such as increased operation and
19 maintenance expense and capital additions to plant in service. The Company has
20 also included several new items such as an increase for the results of a
21 depreciation study that was completed in 1997 and a request for the establishment
22 of a storm reserve, both of which WMECO asks the Department to approve. The
23 Distribution component also includes costs of various public policy initiatives

1 such as conservation and renewables, the levels of which are mandated by the Act.

2 The response to Data Request AG 15-1 provides the components of the
3 Distribution revenue requirements and also provides a comparison with
4 distribution costs that were included in the D.P.U. 91-290 cost of service study.

5
6 Q. Why is it appropriate to set WMECO's Distribution charge as proposed by the
7 Company?

8 A. As shown in the response to Data Request AG 15-1 the vast majority of the
9 change in costs, \$24.7 million, over the seven year period from WMECO's last
10 rate case (D.P.U. 91-290) are related to known and measurable changes, such as
11 increased plant in service (\$6.7 million) and related depreciation (\$7.7 million),
12 property, excise or payroll taxes (\$3.3 million), or new costs; such as those related
13 to revenue requirements mandated under the Act (i.e., renewables charges (\$2.8
14 million)). Such known and measurable changes have been traditionally allowed
15 in the Department's rate setting practices. WMECO believes the Distribution
16 rates set forth in the **Revised** Plan, which reflects the 1998 revenue
17 requirements, achieves the directive to unbundle the rates currently in effect into
18 distinctive components while maintaining a cost of service basis that is required
19 by accounting principles that pertain to a regulated entity.

20
21 Transmission Revenue Requirements

22 Q. How are the 1998 Transmission revenue requirements developed?

23 A. The 1998 Transmission charge proposed in the **Revised** Plan is developed on a

1 cost basis also and is comprised of the resulting transmission charges from NU
2 Tariff No. 9 and the NEPOOL tariff. While neither of these tariffs have yet been
3 approved by FERC, they have been accepted subject to the issuance of further
4 orders, and the NEPOOL tariff has been accepted subject to refund. The
5 Company proposes to reconcile any difference between the transmission rate that
6 is charged to retail customers and the rate that is ultimately approved by FERC.

7
8 Standard Offer Service Energy

9 Q. Please discuss the calculation of the Standard Offer Service level reflected in
10 WMECO's Revised Plan.

11 A. WMECO has adopted the same retail price path for Standard Offer Service energy
12 as those filed initially by other Massachusetts electric companies. The price path
13 begins in 1998 at 2.8 cents per kilowatt-hour and escalates ~~atto~~ to preset levels for
14 the following six years. As further required by the Act, Standard Offer Service
15 will be offered over a seven-year period, beginning March 1, 1998, through a
16 competitive bid process, open to all bidders and administered by an independent
17 third party retained by WMECO. (Please see Mr. Long's testimony filed with this
18 submittal for a more complete explanation of WMECO's Standard Offer Service
19 Solicitation.) Competitive supply of Standard Offer Service will be obtained after
20 the Department approves the solicitation process proposed by WMECO and after
21 WMECO's non-nuclear generating plants (excluding Northfield Mountain and
22 related facilities) are divested and the Northeast Utilities Generation &
23 Transmission Agreement ("NUG&T") modifications are approved by the Federal

1 Energy Regulatory Commission. Until the NUG&T is modified and WMECO's
2 non-nuclear plants are divested, the Standard Offer Service will be supplied on an
3 interim basis from NU system generation resources, pursuant to the NUG&T.
4 WMECO asks that the Department review and approve the solicitation process for
5 the supply of Standard Offer Service and the interim supply arrangement.
6
7

8 Q. Is WMECO proposing to have its generating units "backstop" the supply of
9 standard service at pre-set prices?

10 A. No. As described in its submittal on May 15, 1998, WMECO proposes to remove
11 the backstop obligation from its generating facilities and to solicit its supply for
12 Standard Offer Service from the competitive market without a ceiling price. This
13 modification of the Company's proposal was made to overcome problems that
14 caused other solicitations to be unsuccessful. WMECO has made this proposal on
15 the expectation that it will be allowed to defer and subsequently securitize the
16 difference between the price the Company receives from retail customers and the
17 cost to procure and deliver the required energy and capacity. WMECO asks that
18 ~~seeks~~ the Department's **allow the Company to defer these costs and to rule that**
19 **these deferred costs qualify as transition costs so that they will be eligible for**
20 **securitization, which will be reviewed in a subsequent proceeding.**
21
22
23

1 Transition Charge

2 Q. Please discuss the calculation of the Transition or stranded cost charge component
3 that is proposed in WMECO's Revised Plan.

4 A. As WMECO describes in the Revised Plan, Section IV, the identification,
5 calculation, accounting and mitigation of transition costs are critical elements of
6 the Plan. This testimony provides an overview of the process that was undertaken
7 to accomplish these steps. Please refer to the aforementioned Section IV and
8 Exhibit 13E in the Revised Plan for more information.

9
10 WMECO has identified costs that qualify as transition costs and that are
11 recoverable under the Act's definition of net, non-mitigable commitments which
12 were undertaken to provide electricity to customers. These non-mitigable costs
13 have been categorized into two components, fixed and variable. The fixed
14 component has two main areas - one is related to unrecovered plant asset balances
15 as of December 31, 1995 (including capital additions committed to as of that date)
16 depreciated through the effective date of retail choice (March 1, 1998) including
17 the effects of deferred income taxes. The other is comprised of net unrecovered
18 regulatory assets.

19
20 The variable component contains transition costs that are income statement-
21 related and may vary over time such as nuclear decommissioning costs, the over-
22 market value of purchased power, nuclear costs independent of operation and, in
23 1998, the cost to supply the standard load of WMECO's customers that exceeds

1 3.2 cents per kilowatt-hour.

2

3 WMECO has provided a projection of both the fixed and variable transition
4 charge for the years 1998 through 2010 and proposes to reconcile the variable
5 component on an annual basis. The calculation of the transition charge including
6 a more detailed description of the fixed and variable components are found in
7 Section IV of the Revised Plan and in the text that precedes the schedules in
8 Exhibit 13E. A discussion of the reconciliation process is found later in my
9 testimony.

10

11 Q. You have indicated that WMECO has included only the non-mitigable
12 commitments in its transition charge. Please describe what steps WMECO has
13 undertaken to mitigate fully its cost recovery request as required by the Act.

14 A. As discussed in Mr. Forsgren's testimony, WMECO has committed to, and indeed
15 has already begun, the process of divesting its ownership in its non-nuclear
16 generation assets as specified by the Act. The Company intends to have
17 completed the divestiture of all of its non-nuclear facilities, exclusive of its 19%
18 percent ownership share of the Northfield Mountain Pumped Storage facility
19 ("Northfield Mountain") and related fossil/hydro assets (i.e., Cabot Station and
20 Turners Falls) within six months of the initial offering (August, 1998) and will
21 divest the remainder (e.g., Northfield, Cabot and Turners Falls) no later than
22 January 1, 2000. The reason for separating the auction is discussed in Mr.
23 Forsgren's testimony. When divestiture of these units is complete, WMECO will

1 include the value of any net proceeds over net book value realized through
2 divestiture as an offset to its transition charge. Also, in the event that WMECO
3 can successfully auction its nuclear facilities, which it has committed to divesting
4 by January 1, 2004, any net proceeds from this auction will be applied against the
5 unrecovered balance of transition costs.

6
7 Q. What are WMECO's projections of the revenue requirements associated with
8 transition costs?

9 A. Exhibit 13E has modeled divestiture with proceeds for the fossil/hydro assets
10 equal to the net book value and securitization as of January 1, 1999. When these
11 activities are completed, the Company will true up its transition charge to reflect
12 actuals.

13
14 Q. Does WMECO consider securitization a means of mitigation?

15 A. Yes. The Company's Revised Plan depends upon the savings, or mitigation
16 effect, of securitization in order to achieve the mandatory rate reductions in a
17 financially viable manner. However, as indicated in the Department's rulings
18 regarding the scope of this proceeding, the actual review of WMECO's
19 securitization proposals will be done in a separate docket. In this proceeding,
20 WMECO seeks the Department's ruling that the costs it seeks to recover qualify
21 as transition costs and that WMECO has mitigated these costs appropriately, so
22 that such costs will be eligible for securitization later. Upon completion of
23 securitization, the savings will be applied against the remaining transition costs.

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Q. Are there other means of mitigation that the Company is undertaking in addition to divestiture and securitization?

A. Yes, until WMECO has completed divestiture of its non-nuclear assets, exclusive of Northfield Mountain and related facilities, it will continue to serve its customer load from its own generating units. As such, WMECO's generation costs continue to be pooled with those of other NU companies, through the NUG&T agreement, albeit on an interim basis, which results in the continuation of a net credit against WMECO's transition costs. Additionally, because the Company intends to auction its Northfield and related facilities at the same time as the majority owner, Connecticut Light and Power Company ("CL&P"), WMECO has included that facility as a purchased power contract until completion of that auction. WMECO has proposed this treatment for Northfield because it believes that the sale of its minority interest in the unit would bring a higher price if it is sold concurrent with the sale of CL&P's majority interest. Northfield Mountain and related facilities are projected to provide a benefit to the transition charge during this interim period before they are sold. Further, as Mr. Wiater discusses in his testimony, the Company has proposed to implement a performance based sharing of economic benefits associated with its operating nuclear investments as a means of mitigating its transition costs. In effect, these two proposals relating to unsold hydro and to nuclear plants respectively capture the mitigation value of these units in the competitive generation market during the period before these

1 facilities are sold. The Company is also actively engaged in discussions to
2 renegotiate its two contracts with independent power producers. If buy-down or
3 buy-out of these contract(s) is successful, savings will be used to offset the over-
4 market costs of these contracts currently included in the transition charge. Section
5 V of the Revised Plan discusses more fully the mitigation steps indicated above.
6 Exhibit 13E provides the estimated benefits of these mitigation efforts.

7
8 Q. Regarding the nuclear performance plan, how will WMECO obtain revenues for
9 the output of these facilities?

10 A. WMECO's Plan calls for selling the available output of these facilities into the
11 wholesale market. WMECO plans to maximize the revenues from this sale by
12 offering entitlements in the available energy and capacity of Millstone 2 and 3 for
13 a period starting on the date that Standard Offer Supply is competitively sourced
14 (or, for Millstone 2, the date the unit returns to service if later than the date that
15 the Standard Offer Service is competitively sourced) and ending no later than
16 January 1, 2004.

17
18 Q. The Company recently announced the early retirement of its Millstone 1 nuclear
19 facility. What impact does this have on the Company's stranded costs and how
20 has it been reflected in WMECO's restructuring plan?

21 A. Prior to the July 24, 1998 effective date of the retirement of Millstone 1,
22 WMECO had included the unrecovered cost of plant associated with that unit in
23 its fixed component with recovery over the projected remaining life of the asset

(approximately 12 years). With the decision to retire Millstone Unit 1, the entire unrecovered investment has been categorized as a regulatory asset including the final unrecovered nuclear core, materials and supplies and the projected costs that will be incurred prior to approval to begin decommissioning of the unit (expected by January 1, 2000). Under the Company's Revised Plan, WMECO requests recovery of the Millstone Unit 1 regulatory asset with a return over 12 years beginning July 24, 1998. WMECO seeks that Department's allowance of any unrecovered balance to be qualified as transition costs. WMECO would subsequently seek securitization approval for these costs. The effect of the retirement of Millstone Unit 1 on the transition charge has been included in Exhibit 13E.

Q. Could you describe in detail the cost components for Millstone 1 that are included in the transition charge both before and after the effective retirement date of July 24, 1998.

A. Yes. Prior to the retirement date (i.e., the period March 1 through July 23, 1998) WMECO reflected in the transition charge both a return on and of its unrecovered investment of Millstone Unit 1. The unrecovered investment was the amount of investment as of December 31, 1995, including capital additions committed at that point in time, depreciated through February 28, 1998, with recovery over the remaining expected life of the unit. In addition to return on and of the investment and the associated deferred income taxes, the Company also included certain ongoing costs. These were the annual costs of decommissioning, unavoidable

1 operating costs of the unit such as property taxes, insurance, NRC fees, and other
2 anticipated ongoing operation and maintenance expenses. Finally, until
3 retirement, WMECO's Millstone 1 costs were included in the NUG&T and thus
4 received the credits associated with the allocation of system costs for this unit.

5 **After retirement, such costs will no longer be treated in the NUG&T.**

6
7 With the retirement of Millstone 1, WMECO has requested recovery including
8 return on and of the regulatory asset over a 12 year period. The regulatory asset
9 represents the unrecovered investment of the unit as of the date of retirement
10 (July 24, 1998). In addition to the unrecovered plant investment, the regulatory
11 asset includes the balance of unrecovered materials and supplies and nuclear final
12 core, and the estimated amount of operation and maintenance expenses that will
13 be incurred prior to receiving approval to begin decommissioning the plant ("pre-
14 decommissioning O&M" or "post-shutdown O&M"). An initial 12 year recovery
15 of the Millstone 1 regulatory asset is reflected in the transition charge with the
16 expectation that any unrecovered balance will be subsequently securitized and
17 recovered over the period of the rate reduction bonds. For modeling purposes,
18 Exhibit 13E has assumed that this will be January 1, 1999. In addition to the
19 regulatory asset the Company has included in the transition charge the annual
20 levelized cost of decommissioning the unit. Details of the Millstone 1 regulatory
21 asset and decommissioning cost can be found on page 6A and 8 respectively of
22 Exhibit 13E. The decommissioning estimate was developed by TLG Services in
23 response to the Continued Unit Operation ("CUO") study. Details of the

1 decommissioning estimate can be found in the response to Data Request AG 14-
2 11.

3

4 Recoverability of Fixed Costs of Existing Generating Facilities

5 Q. What has the Company included in its transition charge for existing generating
6 facilities?

7 A. As indicated earlier, the Company has included the unrecovered investment in its
8 existing generating facilities committed as of December 31, 1995 (depreciated to
9 February 28, 1998) in the fixed component of the transition charge.

10

11 Q. Is it the Company's position that these costs are eligible for recovery as transition
12 costs under the Act?

13 A. Yes. First, they are recoverable under Section 1G(b)(1)(i) of the Act, which
14 includes as a category of transition costs:

15 the amount of any unrecovered fixed costs determined by the department
16 for those costs and categories of costs for generation-related assets and
17 obligations to have been prudently incurred and associated with producing
18 electricity from existing generation facilities which were being collected
19 in department approved rates on January 1, 1997, and that become
20 uneconomic as a result of the creation of a competitive generation market,
21 in that these costs may not be recoverable in market prices in a
22 competitive market
23

24 Q. What is the basis of the Company's position that these costs are recoverable under
25 Section 1G(b)(1)(i) of the Act?

26 A. First, all of these costs have been prudently incurred and included in Department-
27 approved rates on January 1, 1997, and are associated with producing electricity

1 from existing generation facilities. Second, all of these costs became uneconomic
2 as a result of competition in the retail electricity market.

3
4
5 Q. Please explain each of the two points in your preceding answer.

6 A. First, the Department has determined in previous proceedings (~~D.P.U. 91-290~~)
7 that the costs of these generating facilities have been prudently incurred or that the
8 rates which include these costs were just and reasonable. The Company provided
9 in several data responses the plant balances for generating facilities that have been
10 approved by the Department for inclusion in rates. Specifically please refer to the
11 responses provided to Data Requests DOER 1-28 and DTE 2-1. Effective rates
12 since D.P.U. 91-290 have been based on two settlements that were in effect from
13 June 1, 1994 through February 28, 1996 and March 1, 1996 through February 28,
14 1998, respectively. The financial analysis upon which the Company entered into
15 these settlements included the projected fixed costs of generating facilities. Given
16 the Department's approval of these settlements these costs have been included in
17 rates WMECO's proposed transition charge. WMECO believes that these
18 findings by the Department are sufficient to meet the requirements of the Act for
19 qualifying transition costs for recovery.

20
21 Q. Please explain your second basis, that it is the Company's position that the
22 unrecovered fixed costs related to existing facilities are now uneconomic as the
23 result of the creation of a competitive generation market.

1 A. It is clear that, as a result of emergence of competition in the generation market
2 WMECO's generating investment will no longer be under full cost of service
3 regulation. Under cost of service regulation, prudent investment can be recovered
4 and thus, it is not uneconomic to its owner. As noted above, WMECO's
5 investment has already been found prudent. Under competition, no assurance of
6 investment recovery is presumed or preordained. Thus, generation competition
7 by its very definition is the antithesis of cost of service regulation and therefore
8 the act of switching from regulation to competition requires the conclusion that
9 any prudent investment made under regulation that is now uneconomic qualifies
10 as transition costs. For prudent investments, the issue then becomes the extent to
11 which investment rendered uneconomic would not be recovered in a competitive
12 market.

13
14 At the present time, unrecovered costs of Massachusetts' utilities investment in
15 nuclear power plants have been rendered uneconomic as a result of competition.
16 As is the case with other electric companies' restructuring plans, the initial fixed
17 portion of the transition charge is based on the presumption that the nuclear units
18 have no economic value. Like the other electric companies' restructuring plans,
19 the WMECO proposal is designed to make the zero value for nuclear plant a
20 presumption only and to credit to customers any future value that the nuclear
21 plants may have. Customers under WMECO's plan will receive credit for the
22 value of the nuclear facilities in two different ways: (1) prior to divestiture by
23 reducing the variable component of the transition charge in proportion to the net

1 revenues (revenues in excess of operating costs) produced by the nuclear
2 facilities, and (2) after divestiture by crediting any value that the plant obtains
3 from the sale at that time against the transition charge.

4
5 Q. Has the Department approved the assumption that nuclear plant has a zero market
6 value in other electric companies' restructuring orders.

7 A. Yes. In all of the electric restructuring cases decided by the Department, an
8 electric company was allowed to recover in the fixed component of its transition
9 charge the full unrecovered cost of its investment in nuclear plant. WMECO
10 requests the same determination in this proceeding.

11
12 Q. Has the value of WMECO's Millstone nuclear generation has been diminished
13 due to the Company's mismanagement?

14 A. No, it has not. However, regardless of how the Company's prior management of
15 its Millstone nuclear generation assets may be characterized, the value of the units
16 now is unrelated to past management.

17
18 For Millstone 3, the largest of the Millstone units, WMECO has spent significant
19 amounts at shareholder expense to restore the unit to a state-of-the-art facility.
20 This effort was rigorously scrutinized by the NRC. Whatever the impact of past
21 practices at the unit, the most recent efforts of WMECO have, at shareholder
22 expense, "washed-out" and made irrelevant any adverse impact of those practices.
23 When sold or valued, Millstone will fetch a price reflecting its current prudent

1 management and the huge shareholder investment WMECO has made to
2 maximize the its operational characteristics with regard to safety and economics.

3
4 For Millstone 2, the second largest of the Millstone units, the same process that
5 brought Millstone 3 back to operational status is now ongoing. Expected to be
6 operational by the end of the year, the value of the unit will reflect, as does
7 Millstone 3, the immense sums being spent at shareholder expense to make the
8 unit an excellent, safe, performer. Past management practice is irrelevant in
9 valuing Millstone 2.

10
11 As indicated previously, WMECO intends to auction Millstone 2 and 3 (the units
12 which constitute the great majority of WMECO net book value) by January 1,
13 2004. When the units are sold, the Department will review that sale an the
14 proceeds received therefrom to determine the reasonableness of the transaction.
15 Thus, the Department will maintain oversight of this issue.

16
17 Millstone 1, by far the oldest and smallest of the Millstone units, has been retired
18 as of July 24, 1998. This decision to close the unit, however, is completely
19 unrelated to past management practices. WMECO and CL&P could have made
20 the unit operational but the CUO study performed by the Company (and testified
21 to by Mr. Wiater), in combination with other considerations (and testified to by
22 Mr. Morris), shows that Millstone 1 has become uneconomic in the generation
23 market. Importantly, the CUO study excluded the adverse effects and start-up

1 costs associated with the non-operational status of Millstone 1. The decision in
2 regard to continued operation of the unit was based solely on the age and size of
3 the unit, its expected operational costs and the forecasted price of power in the
4 competitive generation market. Because the unit could not be expected to
5 compete in the competitive market, it was shut down.

6
7 Q. Does the Company's decision to retire Millstone 1 change your opinion on the
8 Company's right to obtain transition cost recovery?

9 A. No. WMECO's share of Millstone 1 was originally reviewed by the Department
10 and placed in rates after it began commercial operation in 1970, and has been
11 included in WMECO's rates in every rate proceeding since that time. The
12 decision, made in July 1998, to retire this unit does not alter the fact that the
13 investment made previously was deemed prudent. In addition to having been
14 prudent when made, the Company's investment in Millstone 1 was rendered
15 uneconomic due to competition, given the marginal positive value indicated by
16 the economic analysis described in the testimonies of Messrs. Morris and Wiater
17 under the very low risk conditions of a cost of service form of regulation.
18 Continuing to operate such a marginal plant under the higher risk conditions of a
19 competitive environment could not be justified. With regard to Millstone 1, the
20 Company's analysis presented in this proceeding demonstrates that, even if more
21 recent vintage nuclear plants ultimately will have a market value in the future,
22 given the vintage of Millstone 1, and its inherent operating characteristics,
23 Millstone 1 will not have a positive market value in the high risk competitive

1 environment of the future.

2

3 Q. Apart from the fact that the Company believes the unrecovered costs associated
4 with its nuclear plant are eligible for transition cost recovery under
5 Section 1(G)(b)(1)(ii), does the Company have any other grounds for believing
6 that such costs are eligible for transition cost recovery?

7 A. Yes. The Act, of course, provides for recovery of transition costs in various
8 sections. However, the Act specifically allows recovery of investment in nuclear
9 entitlements, which is essentially the nature of WMECO's investment in the
10 Millstone units. Section 1(G)(b)(1)(ii) provides that one category of allowable
11 transition costs recovery is "nuclear entitlements by those electric companies
12 which have divested their non-nuclear generation facilities pursuant to
13 Section 1AY." This provision recognizes the unique nature of nuclear-plant-
14 related transition costs and allows recovery for all such costs without the need to
15 make a further showing.

16

1 **IV. DEFERRALS AND RECONCILIATION MECHANISMS**

2 Q. Are there specific deferrals for which the Company is requesting approval in this
3 proceeding?

4 A. Yes. In order for WMECO to maintain financial viability and still meet the
5 required rate decreases as ordered by the Act, WMECO seeks approval to defer
6 certain costs and seeks approval that those deferrals qualify as transition costs that
7 will be eligible for securitization in a subsequent proceeding. If approved as
8 submitted, WMECO believes that its Revised Plan would enable the Company to
9 meet necessary accounting standards and other financial criteria.

10

11 Q. Can you please describe the deferral requests.

12 A. First, for the period prior to divestiture, WMECO will be supplying energy to its
13 retail customers with its existing generation. Therefore, during this period
14 WMECO has included a base level of estimated costs associated with that
15 generation (see Exhibit 13E, page 3, column N) and requests that it have the
16 ability to defer and subsequently collect any costs incurred over those reflected in
17 Exhibit 13E. Correspondingly, if the actual cost of generation that is incurred in
18 serving that load is below that estimated in Exhibit 13E, then WMECO requests
19 that it be able to apply the over collection to any outstanding deferral balance until
20 such balance has been fully recovered. If there remains a balance of over
21 collection after all outstanding deferrals are extinguished, then the Company
22 proposes that it refund the remainder to customers over a one year period in a
23 subsequent transition charge.

1
2 Second, WMECO requests that it be allowed to defer and recover later the
3 difference between the standard offer energy price charged to its retail customers
4 and the market price that is ultimately paid by WMECO to the supplier of that
5 standard offer. This expected deferral is shown on Exhibit 13E, page 2A, and the
6 transition charge shown in that exhibit assumes those deferrals are securitized.

7
8 Third, the Company requests deferrals necessary to provide full recovery of the
9 cost to serve in 1998 given the constraints of the price cap. As shown in
10 Exhibit 13E, the Company has provided two schedules calculating the 1998
11 transition charge, Schedule 1 and Schedule 2. In Schedule 2 the Company has
12 calculated a transition charge for 1998 of 3.18 cents per kilowatt-hour. Because
13 the Company is capped on its overall rate for 1998, the required transition charge
14 cannot exceed 31.8 cents. As a result, WMECO would not be able to fully collect
15 its anticipated costs, thus resulting in a lower return on equity on investment of
16 10.7% as shown on page 12 of Exhibit 13E, Schedule 2. (This calculation already
17 captures the deferral requested related to the additional July 1, 1998 rate reduction
18 proposed on May 15, 1998 as shown in Exhibit 13E, Schedule 2, page 3, column
19 O.)

20
21 The Company requests to defer the amount of costs that will restore the
22 ~~X.XX~~11% percent return on equity that is foregone, as calculated in Schedule 2,
23 and recover this amount in 1999 to the extent there is room under the capped rates

1 after inflation. Schedule 1 illustrates this by increasing the deferral in 1998 for
2 this item by \$633,000 shown in Column O on page 3. The Company proposes to
3 include the amount for recovery in 1999, also shown in Column O, but has not
4 included that in Exhibit 13E at this time because it is not certain such treatment
5 can be accomplished under the rate cap. As indicated above, to the extent that
6 costs are lower than expected to serve standard service the lower costs will be
7 reflected as a reduction to the transition charge in 1999.

8
9 Q. Does the Company believe that these deferrals can be considered transition costs
10 and, if so, on what basis under the Act?

11 A. Yes. WMECO believes that the costs it proposes to defer be considered
12 regulatory assets associated with generation, pursuant to Section 1G(b)(1)(iii) of
13 the Act. The costs that WMECO defers will be generation related costs that can
14 become regulatory assets after receiving an order from the Department permitting
15 their deferral. Also these costs can be considered the equivalent of over market
16 purchased power expenses related to the supply of standard service for the interim
17 period before competitive supply is implemented. Thus, the Department could
18 approve these costs as transition costs under Section 1G(b)(1)(v).

19
20 Q. Is deferral and recovery of these costs necessary for WMECO to meet the
21 mandatory price reductions in a financially viable manner?

22 A. It will be very difficult for WMECO to provide the price reductions mandated by
23 the Act and maintain financial viability without these deferrals. The Company

1 believes that the Act (Section 1G(c)(3 and 4)) provides the Department the
2 ability to approve such deferred cost treatment due to this circumstance.

3

4 Q. The Company will supply generation for the Standard Offer Service prior to
5 divestiture of its units. How has this been accounted for in the transition charge?

6 A. The Company has included in its transition charge calculation the cost it expects
7 to incur in serving its load up until divestiture of its non-nuclear generating units
8 (excluding Northfield Mountain and related facilities). The projected costs have
9 been reflected on page 3 of the transition charge under column N - Generating
10 Operating Costs.

11

12

13 Q. When does the Company plan on filing the reconciliation of the variable
14 component, including any deferral true-ups?

15 A. WMECO proposes to file the first variable component true up by June 1, 1999 for
16 inclusion in the rate change effective September 1, 1999. This first reconciliation
17 will true up 1998 estimates to actuals for the variable component of the transition
18 charge and also the transmission charge for 1998. 1998 actuals will be known by
19 April 1999. A June 1, 1999 filing will include only a true-up for 1998 costs. The
20 Company then proposes to make another filing by November 15, 1999 which will
21 true-up 1999 costs to the extent known (i.e., 9 months of actual and 3 months of
22 estimates) for effect with the next annual rate change¹. Subsequent to 1999 the

¹ The Company interprets the Act to mandate annual rate changes, after 1999, on January 1 of each calendar year coincident with the change in conservation and renewables charges and the

1 Company proposes to make one annual reconciliation filing by November 1 of
2 each year reflecting 9 months of actual, 3 months of estimates and adjusting for
3 any prior period estimates at that time.

4
5 **V. INCENTIVE MECHANISM**

6 Q. Why is the Company proposing a mitigation incentive proposal?

7 A. The General Court stated in the Act that all reasonable steps should be taken by
8 companies to mitigate their transition costs and encouraged them to divest their
9 generating assets. The Company also believes that an incentive mechanism will
10 meet the Department's and the Legislature's intent that an incentive mechanism
11 will result in lower transition costs and, therefore, ultimately provide benefits to
12 customers through lower rates. In the Eastern Edison Company~~and in Cambridge~~
13 ~~?~~ restructuring case (D.P.U./D.T.E. 96-24) the Department found that an incentive
14 for an electric company to reduce transition costs can be to the benefit of the
15 customers. The Department has noted in other restructuring cases that a mitigation
16 incentive mechanism can motivate a company to seek the highest price for its
17 divested assets while minimizing its transaction costs in doing so. Further,
18 renegotiating above-market IPP contracts more aggressively through an incentive
19 approach could result in lower transition costs and would benefit customers.
20 WMECO's proposed mitigation incentives are directly linked to actual mitigation
21 results, thereby aligning the financial interests of shareholders and customers with

Standard Offer Service rates.

1 the intent of lowering transition costs and benefiting customers.

2

3 Q. What level of mitigation incentive is the Company proposing?

4 A. WMECO proposes that the mitigation incentive be set at 4 percent of the net
5 incremental mitigation resulting from the Company's efforts to mitigate transition
6 costs. **Specifically,** ~~To further explain,~~ the Company has proposed a base level of
7 mitigation in its calculation of the transition charge and proposes, to the extent it
8 can exceed that base mitigation level, the Company will retain 4 percent of any
9 excess mitigation amounts.

10

11 Q. What is this incentive based upon?

12 A. The 4 percent incentive is based on the incentive mechanisms approved by the
13 Department in other restructuring proceedings, most recently Cambridge Electric
14 Light Company, Commonwealth Electric Light Company, and Canal Electric
15 Company (D.P.U./D.T.E. 97-111).

16

17

18 Q. What will the incentive be applied to?

19 A. WMECO's proposal for a monetary incentive of 4 percent is to be applied to only
20 that portion of the mitigation that exceeds a threshold level. The Company will
21 set different thresholds for fixed and variable components of the transition charge.
22 For the fixed component of the transition charge, the Company proposes that the
23 threshold be set at the net book value of the generating asset. For the variable

1 component of the transition charge, which consists of above-market payments for
2 power contracts, the threshold will be set at the estimated above-market payments
3 provided in the Company's restructuring plan as filed in Exhibit 13E.

4
5 Any mitigation incentive received for the Fixed Component of the transition
6 charge will be directly linked to the mitigation received for generation assets in
7 excess over the book value at the time of closure on the sale of the asset.

8
9 Incentive mitigation related to the variable component is proposed to be 4 percent
10 of any excess mitigation the Company achieves in reducing the over-market ~~value~~
11 ~~cost~~ of its purchased power contracts with the Springfield ~~Resource Recovery~~
12 Facility (~~need full name~~) and the Mass ~~ASSPower~~ ~~OWER~~ project that is projected
13 in Exhibit 13E, pages ~~4 of 4~~ ~~and 4A~~. Therefore, to the extent that the amount by
14 which the actual excess over-market is less than the base case level, this amount
15 will be multiplied by 4 percent and retained by the Company.

16
17 Q. Has the Company provided illustrative schedules to support its mitigation
18 proposal?

19 A. Yes, pages 4 and 4x of Exhibit 13E provide examples of the proposed incentive
20 mechanism based on the base case information filed in the Revised Plan. Also the
21 text that precedes Exhibit 13E more fully describes the proposal.

22
23 **VI. CONCLUSION**

1 Q. In conclusion, what is WMECO requesting the Department approve regarding the
2 stranded costs included in the Company's projection of its transition charge?

3 A. WMECo asks that the Department approve the Company's determination and
4 calculation of transition costs as filed in Exhibit 13E along with the unbundled
5 components of its rates (i.e., the Transmission and Distribution charges) and
6 permit the deferrals in the Revised Plan to be qualified as transition costs to
7 enable the Company to maintain its financial viability.

8

9 Q. In your opinion has WMECO fully mitigated its transition costs and otherwise
10 fulfilled the requirements necessary for recovery of transition costs and
11 securitization of those costs?

12 A. Yes, I believe WMECO has fully met the requirements of the legislation signed
13 into law on November 25, 1997.

14

15 Q. Will your testimony be supported by additional individuals?

16 A. Yes. There may be instances where more detailed information will be required
17 that is beyond my immediate expertise. In those instances, I will be supported by
18 other witnesses as appropriate. Where possible a supporting witness has been
19 identified, such as Mr. William J. Starr, Director - Taxes, who will be assisting
20 me as needed on specific tax issues. Biographical information for Mr. Starr has
21 been included as Exhibit RAS-46.

22

23 Q. Does this conclude your testimony?

1 A. Yes it does.

1

EXHIBITS

2

TABLE OF CONTENTS

3

4 Exhibit RAS-1 Biographical Material - R. A. Soderman

5 Exhibit RAS-2 List of R. A. Soderman Data Requests

6 Exhibit RAS-3 Revised Plan Table of Contents/Appendices/Exhibits Listing

7 Exhibit RAS-4 ~~Exhibit RAS-5 — Illustrative Incentive Mechanism Schedules~~

8 Biographical Material - W. J. Starr

9